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PACIFIC NORTHWEST Executive

University of Washington
Graduate School of Business
Vol. 1, No. 1 July 1985

Washington's Governor Makes a Case for Economic Development

REGIONWATCH:

- BPA Takes a New Look at Its DSI Rates
- Facts at Your Fingertips: The Annual Economic Indicators

Comparable Worth in the Private Sector

Do Washington's Taxes Hurt New Business?

From the Publisher

The Graduate School of Business Administration is delighted to present the first issue of ***Pacific Northwest Executive,*** *a quarterly business magazine focused on regional economic, managerial, and policy issues.*

The Northwest is undergoing change, and our movement towards a new kind of economy has not been an easy one. At the University of Washington an important part of our mission is to foster an ongoing discussion of economic and business events in order to illuminate the changes we are facing. That's what ***Pacific Northwest Executive*** *is all about. In each issue we'll review important regional economic trends and focus on several key management and policy topics. An annual statistical supplement, included in this issue, will summarize important economic indicators for the Northwest states.*

Pacific Northwest Executive, *funded by a grant from the Seafirst Bank, is one avenue of many by which the Graduate School of Business Administration demonstrates its active involvement in promoting management excellence. In addition to a whole range of executive development programs, we work in partnership with the business community through our Executive M.B.A. Program, the Center for the Study of Banking and Financial Markets, and the Center for Retail, Transportation, and Distribution Management. Our commitment is strong—and it's growing.*

The University is sometimes seen as being detached from the community. We hope that ***Pacific Northwest Executive*** *will dispel that notion once and for all. Our aim is to help the Northwest business community stay informed. In doing that, we fulfill one of the University of Washington's primary goals: to serve our community.*

Nancy L. Jacob

Nancy L. Jacob, Dean
Graduate School of Business Administration
University of Washington

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Cover illustration by Gary Jacobsen

Fostering Economic Development in Washington

by Governor Booth Gardner

PETE KUHNS

As a businessman turned public servant, I came to the Governor's Office with a keen sense that government doesn't always get its priorities straight. State government's responsibilities will always be a matter for legislative and public debate, of course, but I believe one of the paramount problems of our state right now is the utter waste of human resources caused by high unemployment.

There is no shortage of important problems, particularly pollution which threatens Puget Sound and other water resources. Another problem is our unfair, unstable, and inefficient tax system. Economic development can provide the resources we need to help solve some of the state's problems while reducing high unemployment. That's why I've made development a central theme of my administration.

A quick glance at the statistics reveals the most compelling reason why we must act decisively. Currently, 9.5 percent (March 1985 figures) of the state's labor force of 2,069,500 is unemployed; that's 196,603 human beings surviving without a job and using costly social services. The state's labor force is expected to grow by some 664,300 people by the year 2000 (see the table on page 4). If we made no progress in reducing unemployment, the number of people without jobs would rise by almost 60,000 to 243,912—meaning nearly one-third more people would be out of work than today.

An effective economic development program can help break this state's historical pattern of having higher rates of unemployment than the nation as a whole. Washington's unemployment rate has exceeded the national average for the past fourteen years (see the figure on page 4). In economic recessions, our unemployment is up more sharply than it is nationally; when the national economy rebounds, Washington's unemployment does not recover as quickly as the national rate. In addition, in more recent years Washington has borne the brunt of major structural changes in the national and world economies. From statehood, we have been dependent upon natural resource-based industries such as wood products, fishing, and agriculture. Changing technology, resource depletion, and falling prices have hurt many of these industries. Between 1979 and 1983, 127 Washington firms shut their doors for good.

Many of these factors have been beyond our control. Our labor force is no less productive than in the past, and the managers of our industries are no less competent. In fact, the opposite is more likely true. We are simply the victims of inevitable change. However, part of the problem has been that government has not been prepared to deal with such radical disruption of the state's economy.

The current recovery has introduced a novel, yet undesirable twist. While the state's economy added jobs by the thousands since 1982, most jobs have failed to go where they are needed most. We find ourselves the inhabitants of "two Washingtons." In one of them—the state's metropolitan areas—prosperity and business expansion are the order of the day. Business activity in the Seattle, Spokane, and Vancouver areas, for example, is running at a feverish pitch. In the "other" Washington, however, movement is in the opposite direction. In places like Grays Harbor County and across the state in the Okanogan, mills continue to close and unemployment, now at 17 and 22 percent respectively, is still growing. We are face to face with a challenge we may not feel equipped to meet, but which can't be ignored.

. . . nearly everything we do in the public sector. . . depends upon the health and prosperity of the private economy, which is the ultimate source of virtually all state revenue.

Few would deny that government has a role to play in resolving the problems of people displaced during unsettling times. The economic well-being of our citizens is one of state government's most pressing responsibilities and the primary justification for economic development programs.

Another important reason why we need an effective economic development program goes beyond the basic human need for jobs. All the things that government provides—education, pollution control, highways and bridges, safety, and public health—demand a state economy healthy enough to generate adequate revenue to pay for them. My administration has not wasted any time getting started on an aggressive new program which seeks to find solutions and get results. I am encouraged by the strength of our momentum just a few months out of the chute.

Twenty days after my inauguration, we proposed the Washington Plan for economic development. The Plan is as basic as nuts and bolts, founded on the belief that the private economy is the engine room of the ship of state. That may sound corny, but nearly everything we do in the public sector—whether it be the cleanup of Puget Sound, or improved education for our children—depends upon the health and prosperity of the private economy, which is the ultimate source of virtually all state revenue. So it makes perfect sense to do everything we reasonably can to allow the economy to flourish and expand. While the Washington Plan has a number of elements, it is essentially a program built around cooperation between public and private sectors across the state in a drive for balanced economic expansion.

The Plan provides a framework, a structure on which to build cooperation in several forms. It also provides a mechanism for rapid response to opportunities and obstacles. It provides for developing a strategic long-term analysis of our state's economy, and it provides a common theme and common direction for all economic development activities.

While it is simple in form, the Washington Plan is ambitious. It promotes the growth of existing business, encourages trade expansion to both offshore and domestic markets, works to attract new manufacturing and assembly plants, encourages tourism, and entices film and video production to the state. Here are the most important elements of the Washington Plan.

► **The Economic Development Cabinet** is our answer to a previous lack of coordination and cooperation among the state's various agencies, many of which are involved in economic development in one way or another. Some have actual economic development programs, while others may have a direct effect upon the success of economic development projects through the exercise of regulatory powers. Normally chaired by me, the Cabinet is made up of

Booth Gardner was elected Governor of the state of Washington in 1984 and took office in January 1985.

Washington State Trends in Labor Force and Unemployment

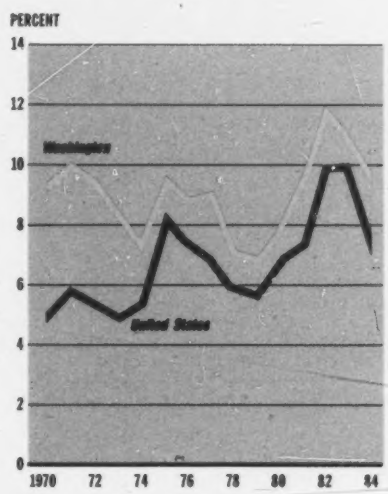
Calendar Year	Labor Force[1]	Labor Force Increase	Persons Unemployed[1]	Increase in Persons Unemployed
1985	2,076,300		184,791	
1990	2,312,600	236,300	205,821	21,030
1995	2,525,100	212,500	224,734	18,913
2000	2,740,600	215,500	243,912	19,178
15-year increases:		**664,300**		**59,121**

[1] Estimated average for entire year

Source: *Washington State Department of Employment Security*

the heads of up to twenty-five state agencies, who typically meet to resolve a specific economic development problem. Occasionally, meetings have a planning purpose such as one recently convened to discuss the Superconducting Super Collider, a U.S. Department of Energy project that we may pursue. More often, a Cabinet meeting may be requested by a company asking assistance for one reason or another in its attempts to move to or expand within Washington. Agencies dealing with a client company independently may be unaware that their actions may be detrimental or discouraging to a company intending to expand in or relocate to the state. The Cabinet meeting assures that all agencies are fully informed of a client's requirements. Agency heads can be expected to cooperate and to expedite action, resolving problems in a matter of hours.

UNEMPLOYMENT RATE
Washington and United States



► **The Special Community Action Team** also depends on interagency cooperation. This program is under the direction of the Department of Community Development, headed by Dick Thompson, who understands both economic development and community needs. The Team will be comprised of representatives from state agencies that can offer either expertise or specific economic development remedies to a community in need. As I conceive the Team, it will provide a coordinated state response to communities which are economically distressed due to natural disaster, unanticipated economic disaster (such as a major mill closure), or chronic unemployment.

► **Team Washington,** the most ambitious element of the Washington Plan, is fast emerging as a true cooperative partnership between public and private development agencies across the state. Team Washington involves the Department of Commerce and Economic Development as lead agency. The department has been reorganized into two groups: the Washington Outreach Group, responsible for domestic and international plant recruiting, tourism, and film/video recruiting; and the Washington Business Assistance Group, aimed at helping existing businesses survive and expand, and supporting the outreach effort by encouraging domestic and international trade, providing technical services to support development efforts, and offering small business services not being provided by other state agencies.

But Team Washington is much more than a new organizational structure for the Department of Commerce and Economic Development. It's a consulting and marketing organization composed of private development agencies across the state—called Associate Development Organizations—working together under the department's leadership. To date, agencies representing fifteen of Washington's thirty-nine counties have signed up as Team Washington members. Also, one of the first to sign on was the Economic Development Partnership for Washington, a non-profit statewide development agency supported by business.

These organizations sign agreements with the Department of Commerce and Economic Development in which roles, coordination, and procedures are outlined, including the process for acquiring and managing plant investment prospects and cases. Eventually, we anticipate that every part of the state will participate in Team Washington. Each organization (typically an economic development agency) would receive $25,000 in matching funds, as proposed in the 1985–87 budget submitted to the legislature. Matched by funds or services from the organizations, the money would go to support a full-time staff person at the local level, thus correcting one of our greatest resource deficiencies. Having the ability to call on the resources of offices across the entire state—all operating on a full-time basis—will create an instant, geometric jump in effectiveness for the state's economic development effort. The new organizations will constitute a statewide network providing small business assistance, export assistance, and plant siting assistance.

In addition, the organizations will be invited to join Team Washington missions to expand domestic and international trade opportunities, attract new industry from other states and countries, encourage tourism to Washington state, and obtain sales opportunities from the federal government. Some of these missions will involve my personal participation when the office of the Governor can make a difference in obtaining results.

A final element of Team Washington is the Washington Ambassador Program, which is the responsibility of the Economic Development Partnership for Washington,

the previously mentioned private sector non-profit organization. Some 150 volunteer business executives from across the state will soon be going through a training program to prepare them for their mission as Washington Ambassadors. Their mission will be to make coordinated sales calls on the state's investment and trade clients overseas, in the course of their own travels. Through their business contacts, the Ambassadors will also collect intelligence on plans by growing companies to locate plants or other facilities in the United States. In the fast-paced world of industrial recruiting, timely knowledge of the market is crucial. I expect the Ambassador program to give us an edge on the competition.

That's the structure of the Washington Plan. It is a description of an organization, but, as we all know, people make the difference. The people who will make the Washington Plan and Team Washington work, led by the Department of Commerce and Economic Development Director John C. Anderson, are qualified economic development professionals. John Anderson worked closely with me to develop the Washington Plan, and I am confident he is the best economic development professional to carry it out. I have asked the Washington State Legislature to give his department the tools it needs to achieve real results.

The legislature has responded positively during its regular session. Members successfully passed a number of bills important to our new economic development initiatives. I have signed measures which accomplish the following:

► Provide for a major reorganization of the Department of Commerce and Economic Development to allow it to carry out its Team Washington mission. As the state's primary development agency, the department will have the ability to streamline its structure to meet the realities of the modern economic development world.

► Establish the Special Community Action Team within the Department of Community Development, which I have described.

► Provide deferral of sales taxes to investors in distressed areas of the state (defined as a county where average unemployment for the last three years exceeds the average for the state by 20 percent). Fifteen counties are currently eligible. A three-year deferral, with payback over five years, applies to equipment and construction costs.

Economic development can provide the resources we need to help solve some of the state's problems while reducing high unemployment.

► Provide a three-year deferral of sales taxes on construction and equipment for out-of-state manufacturing companies, which locate anywhere in the state. The same five-year payback applies.

► Provide $15 million in new funds for the Community Economic Revitalization Board (CERB). These funds will be used to provide infrastructure facilities such as roads and water and sewer lines, in support of new private sector job-producing investments.

► Establish the Washington State Development Loan Fund, which can be described as a "deal-closer." Money from the fund, administered by the Department of Community Development, may be disbursed in addition to CERB loans or grants for any project and for any reason, with a limit of $350,000 per project. It is funded from federal Community Development Block Grants and $5 million from the state's capital budget.

► Provide additional funds to pay for vocational-technical training for displaced workers in distressed areas of the state. The pilot program provides tuition grants to students at six community colleges.

► Reorient the state's Export Assistance Center as the Small Business Export Finance Assistance Center, providing financial counseling for small business exporters.

► Permanently establish the International Marketing Program for Agricultural Commodities and Trade (IMPACT) at Washington State University. The IMPACT Center is expected to develop practical solutions to problems which impair the marketing of Washington agricultural products.

► Permanently establish the International Center for International Trade in Forest Products at the University of Washington, which will do for forest products what the IMPACT Center does for farm products.

► Set up the Washington State Economic Development Board, whose members will advise the Governor as we finally start developing a long-term economic development strategy for the state. The Board will be chaired by me, and will be made up of legislators from the four legislative caucuses, twelve persons from various economic sectors, and five citizens at-large. Although the process is expected to take several years, my goal is to create a strategic plan which can guide the state's development efforts for years to come.

I believe we have made a good start in only a few months at building an economic development program that will pay off big dividends in the months and years ahead. I am encouraged by the positive attitudes of the legislators, by the professionalism of the economic development community, and by the enthusiasm of the general public. Obviously, our program is ambitious, and it must be. It is also imaginative and different from what has been tried in the past, and it must be. Previous state efforts have not been effective. Our program is aggressive because the climate for economic development has become much more competitive. We must be assertive in what is today an investor's market.

All of this effort will be worthwhile if, with public support, we can re-employ a large percentage of the almost 200,000 Washington citizens still looking for a job. We can't accept two Washingtons. Our success will not only help the jobless, it will also diversify our economy and lower the state's cost of providing social services. The money and energy we expend will be worth it if our program builds new public revenues—not only to alleviate the pressure on our current tax system, but also to pay for a growing demand for public services. I hope that the business community will join with me as members of Team Washington to support our economic development efforts. For while we are off to a fast start, we have many more miles to run.

REGION WATCH

Economic Developments in the Pacific Northwest

The Pacific Northwest is a magnet attracting new residents and new enterprise. Sometimes the pace of economic development appears too rapid, straining the absorptive capacity of our infrastructure and environment. The 1980s, on the other hand, appear to be a period in which the growth of income, production, and employment in the Pacific Northwest is falling short of expectations formed on the basis of long-term trends. Recent growth rates, measured either in terms of real income or employment, have slackened significantly compared to those of the previous two decades. Not only are growth rates below trend, so far this decade they have even fallen short of national expansion rates. During 1984 the U.S. economy experienced growth of a dramatic dimension, and nationally real personal income rose by 6.4 percent. The Pacific Northwest states shared in this expansion, but the pace of growth was unusually modest. Washington real personal income rose only 2.6 percent. Real personal income in Oregon and Idaho rose 4.7 percent and 4.6 percent respectively, but these rates represent a reaction to the greater severity of earlier recessions in those states.

Personal income rises modestly

Developments taking place in labor markets of the Pacific Northwest also reflect the sluggish behavior of income growth. Total employment reached record highs in 1984 in Washington and Oregon, and in Idaho total employment barely missed recapturing its previous 1980 peak. Payroll employment rose to 1,640 thousand persons in Washington on an annual average basis, exceeding the prior peak of 1981. Oregon payroll employment rebounded last year to an annual average of 1,004 thousand persons; that was still short of the previous 1980 peak level. Idaho payroll employment during 1984 averaged 326 thousand, also just under its 1980 level. Changes taking place in each state last year were in a favorable direction, and recent monthly reports suggest improvements are carrying forward into 1985, but hardly at a breathtaking pace.

Employment up, but not much

The slow improvement in the employment picture is also reflected in recent unemployment statistics. March unemployment rates in Washington state were below year-before levels; although not officially adjusted for usual seasonal swings, the March rate appears to be about 9.7 percent on a seasonally adjusted basis. Oregon reports a March seasonally adjusted rate of 9.5 percent. The reported unemployment rate in Idaho is typically low, and the seasonally adjusted March rate of 6.5 percent is comfortably below the national rate of 7.3 percent.

Unemployment rates improving

The reasons for slower growth within the Pacific Northwest states are as varied as their mix of industries and markets for products. All have experienced significant electric energy cost increases. For Washington and Oregon, rising energy costs have threatened the competitive position of aluminum smelters vis-a-vis aluminum plants elsewhere. The Martin Marietta plant at the Dalles, Oregon has closed its doors, and other plants are feeling a cost-price squeeze. High real interest rates during the past five years have impacted the housing market nationally and the lumber industry regionally. But even as housing starts have turned favorable, market penetration by Canadian lumber imports and the emergence of Southern states as major suppliers of wood products have sent shockwaves through the Douglas Fir region. In Puget Sound, the shipbuilding industry is in danger of sinking fast. The Tacoma Boatbuilding Company has faced successive financial crises, while Todd and Lockheed are starving for new Navy contracts. Even the Puget Sound Naval Shipyard in Bremerton is trimming jobs as part of a Navy cost reduction program.

Aluminum, lumber, and shipbuilding are struggling

At the opposite end of the bad news/good news spectrum are expanding industries. The "service" industry in Washington is the distinctive growth sector. Oregon, too, has added significantly to its services industry during a period in which its manufacturing base has contracted.

Services are expanding

The term "services" is usually used in a broad sense to include communication, transportation, utilities, wholesale and retail trade, and finance/insurance/real estate services, as well as the more narrowly defined statistical concept of business and personal services. The rapid growth of the service industry at a time when the growth of manufacturing is in remission seems to defy traditional notions that service sector growth depends upon the growth of basic industry. This shift to services is sometimes viewed negatively as evidence of the "deindustrialization" of America, or considered undesirable because the average wage in the service industry is less than the average in manufacturing. The positive aspect of the growth of the service sector is that it contains significant elements of "high-tech" activity, including computer software firms, technical research services, and the knowledge industry, as well as jobs for unskilled workers.

Although no long-term job gainers stand

out among Washington state manufacturers, aerospace recovered from its cyclical low of 62,300 jobs in October 1983, and is currently (April 1985) employing 74,800 persons (see Figure 1). Electrical machinery and electronics has been the stand-out performer in Oregon; last year it added 3,200 workers, bringing the 1984 monthly average to 13,900 jobs. Since 1980 this industry has expanded its payrolls in Oregon at an annualized growth rate of 9 percent, with more growth anticipated during 1985-86.

Employment in aerospace and electronics is climbing

The recovery is not uniformly distributed over the region. The metropolitan areas, particularly Seattle–Everett and Portland, are experiencing more rapid income and employment growth, and lower unemployment rates, than outlying areas. The resource-based counties, more dependent on lumber, aluminum, mining, and agriculture, are not fully sharing in the current recovery.

The central cities fare well

REPERCUSSION ON STATE FINANCES

The impact of sluggish growth in the region is felt acutely in the public sector. The tax base of Washington state has grown less rapidly than previously expected, and has actually declined in Oregon due to a severe recession and slow recovery. Idaho has fared better, with a moderately expanding tax base.

Washington's tax base is climbing from $8.1 billion in the 1983–85 biennium to a mid-1984 forecast of slightly over $10 billion for the 1985–87 biennium. Initial budget and tax planning on the basis of that early, optimistic forecast then had to be revised as later forecasts lowered the 1985–87 revenue forecast to approximately $9.6 billion—still a significant increase over the previous biennium. In addition, the U.S. Bureau of Economic Analysis, which provides personal income estimates to the state's forecasters, has revised its Washington series downward, resulting in a still lower revenue forecast. At the time of writing, the new forecast has not been released, but it is expected to be in the neighborhood of $9.4 billion.

State revenues fall short in Washington...

The sequence of lowered revenue forecasts has made it especially difficult for Washington's new governor to create a reserve fund in the budget. The requested reserve of $300 million was intended to help the state weather a possible recessionary period in the coming biennium, or to compensate for federal budget cuts that are likely to impact the state. It now seems likely that any reserve fund would require a tax increase.

In Oregon, the fiscal problem is of a much more Draconian nature. During the 1983–85 biennium, Oregon's revenues are expected to reach $3.219 billion. However, slow economic growth and structural changes are expected to net only $3.074 billion in the 1985–87 biennium. Drastic cutbacks in state employment and reorganization of agencies are taking place.

...and decline in Oregon...

Tax reform initiatives in Oregon have resulted in removal of the unitary tax on corporate profits, and a referendum will be on the ballot in the fall to establish a sales tax, simultaneously lowering the property tax rate. Thus, the changes in the tax code are not expected to increase the state's revenues, but will redistribute the burden of paying for schools and other services.

Idaho's modest economic growth rate is producing an expanding tax base which affords state executives an easier budget situation. Revenues are expected to grow from $487 million in 1984 to $549 million in 1985 and to $577 million in 1986. This state's revenues seem to be expanding at more than the rate of inflation, allowing for very modest expansion of services.

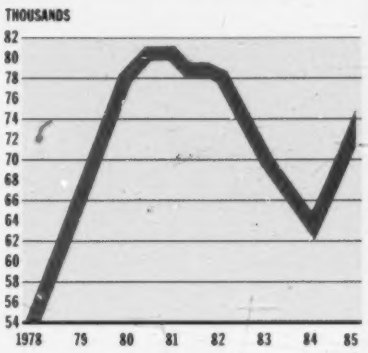
...but rise in Idaho

INDUSTRY DEVELOPMENTS

The *banking* sector is undergoing major structural changes. The Pacific Northwest is participating in a national trend toward liberalization of state restrictions on interstate banking. Idaho, Oregon, and Washington have all passed legislation recently allowing a broader range of acquisitions by out-of-state banks. Interstate banking in Washington has hitherto been limited to emergency situations in which an out-of-state bank is allowed to acquire a troubled bank in order to protect depositors. Seafirst Bank was acquired by Bank of America under such circumstances. Washington's new law, effective in 1987, permits interstate banking on the basis of reciprocity, and allows Washington banks to establish branches outside their home counties (formerly possible only through acquisition of an existing bank). Since Oregon's new law provides for acquisitions by banks within the Twelfth Federal Reserve District, the planned merger of Old National Bank of Washington and U.S. Bancorp of Oregon may now proceed. Also, the Bank of Oregon may be purchased by California-based Bank of America.

Interstate banking is spreading

Figure 1: Aerospace Employment in Washington



The slow recovery from the recent recession has been accompanied by a number of *plant closures* in the Pacific Northwest. Wood products closings have had devastating impacts in several communities. Champion International closed six wood products mills in Oregon and two in Washington. Weyerhaeuser closed three facilities in Washington. Even high-tech plants have not escaped the strains of a recession; Intel put off a major expansion of its Oregon facilities and laid off approximately 500 workers.

Wood mills close

Generally high-tech continues to be a growth industry for Oregon. NEC America has announced a new fiber optics plant for Washington County. Fujitsu plans a new facility at Gresham. National Semiconducter is going to build a chip facility in Oregon and has announced an R&D facility for Portland. Epson American is planning a computer terminal plant in Washington County.

High-tech growth expected

Both Washington and Oregon attempted to attract a new RCA–Sharp joint venture semiconductor plant. Washington won after Governor Gardner persuaded the legislature in its special session to pass a sales tax deferral bill. The bill allows an out-of-state manufacturing company to build a plant in Washington and defer sales taxes on construction and equipment for three years with a subsequent five-year payback. The $200 million RCA–Sharp plant will be located in Clark County, and will initially employ 600 people, with later expansion to 1600 people.

Wage Rates in Washington State

Average hourly earnings of production workers in Washington manufacturing industries are the highest in the continental United States. Not counting fringe benefits (which probably add another 30 to 35 percent to labor costs), production workers in manufacturing averaged $11.56 an hour in Washington in 1984, or 29 percent more than the national average. Industry mix partly accounts for this (e.g., aerospace) but many Washington industries pay more per labor hour than the same industry nationally (see Figure 2). In lumber and wood products, and in pulp and paper, Washington average hourly earnings are reported to be 42 percent more than the national average for these industries. Hourly earnings in chemicals, fabricated metals, and the stone-clay-glass combination tend to run about 20 percent above their respective national industry averages. In shipbuilding, for which industry earnings are not separately reported in official statistics, U.S. Navy contracts are going to shipyards elsewhere where labor rates are significantly lower.

Disparities in average hourly earnings are even wider geographically. In lumber and wood products, to take a pertinent example, average hourly earnings are nearly twice those paid in the Southern wood-producing states (see Figure 3). Such high industry wages may be viewed as a tribute to the productivity of the Pacific Northwest workforce; alternatively, they may be viewed as a cause for concern over the ability of the region to market products in competition with lower cost producers elsewhere. Since there is only fragmentary evidence of productivity differentials, only indirect evidence can tell which view is correct. That evidence takes the form of decisions made by producers who are locating new plants or expanding their operations since they will choose locations where total costs are minimized.

Not surprisingly, spokespersons in several of Washington's basic industries claim they are at a competitive cost disadvantage. The reasons cited are often multiple: in addition to comparatively high labor costs, rising energy costs, high material costs, and increasing transportation costs are most frequently mentioned. Competition from other regions and from foreign producers—in domestic as well as world markets—is blamed. Whatever the causes, these have combined to adversely affect market shares, slow employment growth, and trigger plant closures in several important manufacturing industries. Forest products, steel fabrication, and shipbuilding have been particularly hard hit. Permanent closures of a number of mills in the forest products industry are regrettable reminders of the long-run lack of competitiveness of many Pacific Northwest producers.

For such industries, the return to national competitiveness is a difficult challenge. The greater the producers' losses are, and the longer they continue, the more pressure there is to become cost-effective. . .or quit the business. The higher and more prolonged unemployment is, the greater the pressure for workers to settle for less. . .or move. These unfortunate consequences are especially felt in those communities which do not have a diversified industrial base.

Some cost adjustments are taking place in the labor market, often using novel approaches. For example, dual wage rates, where new employees are hired at wage rates lower than those paid present jobholders doing the same work, were unheard of five years ago. Changes have taken place in plant ownership, with existing labor contracts cancelled or renegotiated. Conversion of some companies to worker-owned cooperatives in which employees buy shares entitling them to jobs, usually at substantial paycuts, has taken place. But it is not easy for workers, whose real wages have failed to rise over the past decade, to accept the fact that shifts in the location of markets, competition from other regions and new products, and rising costs of energy and capital, have cost them part of their wages. . .or worse, their jobs.

The cost picture for some Pacific Northwest industries is quite favorable. In electrical machinery, for example, hourly earnings of production workers in Washington and Oregon are generally less than those in California, and either close to or somewhat under the national industry average. Along with other conditions which are important locational determinants, favorable labor costs here have been a consideration in the attraction of high-tech producers to the Pacific Northwest. But these are frequently low-wage activities compared to aerospace, metals, shipbuilding, and forest products, so that job-for-job the impact on personal income is less.

Figure 2: Percent by Which Washington Wage Rates Exceed National Industry Average
Washington State, 1984

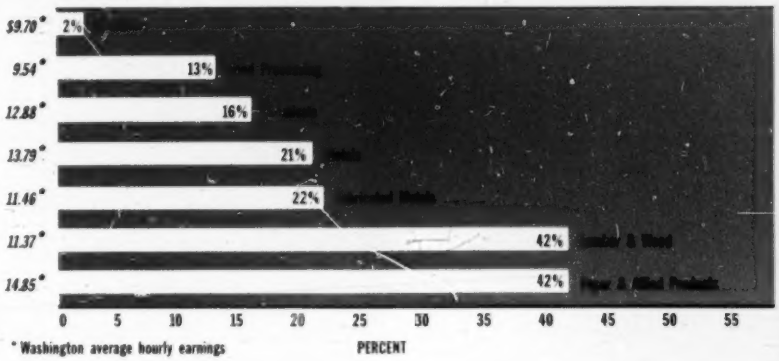
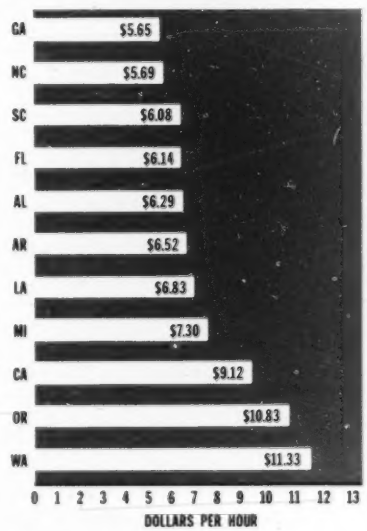


Figure 3: Average Hourly Earnings of Production Workers in Lumber and Wood Products, Selected States, 1983



Economic Forecasting in the Pacific Northwest States

Economic forecasting is a complex technical effort with benefits to decision makers in the public and private sectors. The three Northwestern states of Washington, Oregon, and Idaho all conduct forecasting exercises to predict their revenues. Many private sector organizations also have a staff capability to conduct forecasts, but few of these forecasts are publicly available. For those executives who do not have in-house forecasters, the three state forecasts are among the major sources of information about the probable future condition of the economy.

State Economic and Revenue Forecasting Process

■ WASHINGTON

The forecasting process in Washington (see Figure 4) begins with the forecasting staff in the Department of Revenue who consult a recent national economic forecast. Washington's forecasters usually rely on the Data Resources, Inc. (DRI) national forecast, although some of their most recent forecasts have been based on the Wharton Econometrics forecast. Selected variables from the national forecast are entered into an econometric model of the state. This model was originally prepared for the state by DRI, and is currently maintained and operated by the Office of the Forecast Council. This staff group was formerly located in the Office of Financial Management, but was moved into the Department of Revenue during the Spellman Administration. Simulations conducted with the Washington model result in a preliminary state economic forecast. At this point a two-pronged review begins, involving an Economic and Revenue Forecast Council/workgroup (ERFC) and the Governor's Council of Economic Advisors (GCEA).

The ERFC consists of the directors of the Office of Financial Management and of the Department of Revenue, as well as four legislators representing the House and Senate and both political parties. With representatives of both the executive and legislative branches of government, the ERFC's mandate is to review the preliminary economic forecast, participate in the preparation of the revenue forecast, and to eventually formally adopt the final forecasts of both the economy and state revenues. This body is a somewhat unusual attempt to create institutional unity throughout the state government, avoiding some of the acrimonious debates over revenue forecasts which took place during the last recession. The ERFC was created during the 1984 legislative session and has presided over the preparation of three quarterly forecasts since then.

The preliminary economic forecast is also reviewed by the GCEA, a group of academic and business economists appointed by the Governor. Prior to the quarterly meeting of the GCEA, members complete a questionnaire regarding the variables used as inputs to the state model. The GCEA then meets with the Governor, and, lately, with the new ERFC members in attendance. The exact process followed at these meetings has varied. Usually members are asked to comment about particular variables or aspects of the forecast. At other times, the Governor or ERFC members will query the Council about factors of concern.

Following these reviews, the forecasting staff prepares the final economic forecast, and then proceeds to prepare the revenue forecast. As indicated in Figure 4, not only the Department of Revenue but a number of other agencies are involved in the revenue forecasting effort. The Department of Revenue, which collects over 90 percent of the state's revenues, prepares a forecast of its revenues using a formal econometric model. The other agencies with independent revenue sources prepare the forecasts of these sources, and Department of Revenue staff collates these various forecasts into the final revenue forecast.

■ OREGON

The forecasting process in the neighboring state of Oregon (see Figure 5) is similar in many respects to that in Washington, but has some interesting variations. The forecasting staff is within the Executive Department of the Oregon government. The process starts with a national economic forecast as it does in Washington, but Oregon chooses to rely on the DRI forecast. A preliminary state economic forecast is then prepared by taking variables from the DRI forecast, entering them into a state econometric model, and simulating future condi-

Figure 4: Economic and Revenue Forecasting Process—Washington

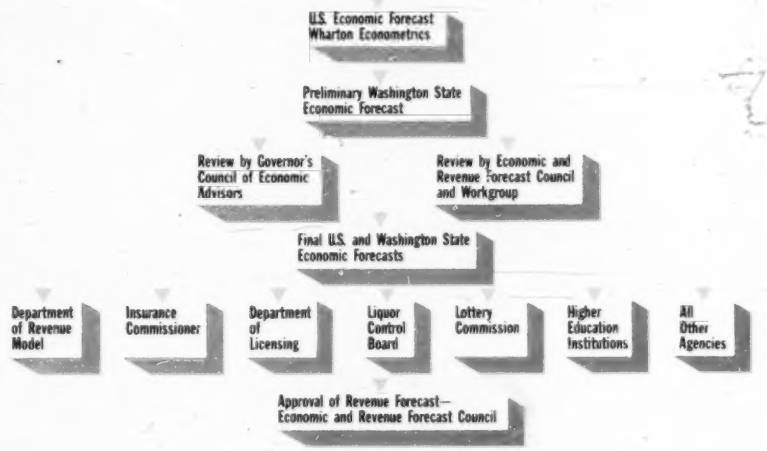
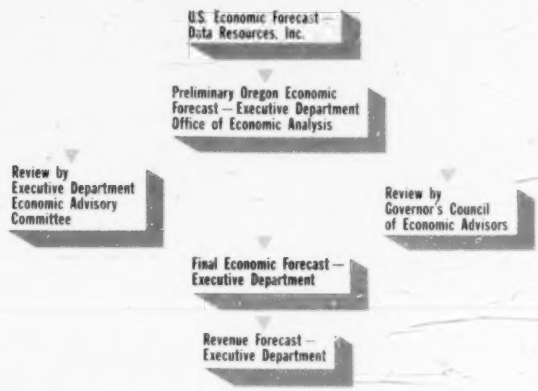

U.S. Economic Forecast Wharton Econometrics
Preliminary Washington State Economic Forecast
Review by Governor's Council of Economic Advisors
Review by Economic and Revenue Forecast Council and Workgroup
Final U.S. and Washington State Economic Forecasts
Department of Revenue Model
Insurance Commissioner
Department of Licensing
Liquor Control Board
Lottery Commission
Higher Education Institutions
All Other Agencies
Approval of Revenue Forecast— Economic and Revenue Forecast Council

Figure 5: Economic and Revenue Forecasting Process — Oregon


U.S. Economic Forecast — Data Resources, Inc.
Preliminary Oregon Economic Forecast — Executive Department Office of Economic Analysis
Review by Executive Department Economic Advisory Committee
Review by Governor's Council of Economic Advisors
Final Economic Forecast — Executive Department
Revenue Forecast — Executive Department

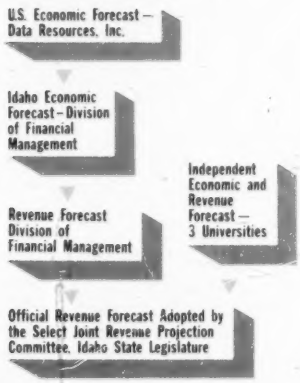
tions in the state.

This preliminary forecast is then reviewed by two groups: the Executive Department Advisory Committee (EDAC) and the Governor's Council of Economic Advisors (GCEA). The EDAC is composed of thirteen agency economists from various parts of the state government. As in Washington, the GCEA consists of a number of academic and business economists. Following review of the economic forecast by these two groups, the forecasters then prepare a final economic forecast. The Executive Department then prepares a revenue forecast, and the results of both the economic and revenue forecasts are published quarterly, just as in Washington.

■ IDAHO

In Idaho the forecasting process (see Figure 6) is considerably simpler than in its neighboring states to the west. The forecast is prepared annually to match the state's fiscal cycle, rather than quarterly as in the other two states. The DRI national forecast serves as the starting point for exogenous variables entered into a state econometric model. The Division of Financial Management runs simulations with this state model to prepare a state economic forecast, and then prepares a revenue forecast without any of the outside reviews conducted in Washington and Oregon. However, the final forecasts of the economy and revenues are then submitted to the Select Joint Revenue Projection Committee of the state legislature. In addition to examining the Division of Financial Management forecast, the Committee conducts hearings at which independent forecasts may be presented.

Figure 6: Economic and Revenue Forecasting Process — Idaho


U.S. Economic Forecast — Data Resources, Inc.
Idaho Economic Forecast – Division of Financial Management
Independent Economic and Revenue Forecast — 3 Universities
Revenue Forecast Division of Financial Management
Official Revenue Forecast Adopted by the Select Joint Revenue Projection Committee, Idaho State Legislature

For about the last ten years, a team of economists from the University of Idaho, Idaho State University, and Boise State University has prepared an independent forecast using an aggregated model of the state economy. Several national forecasts are consulted, and forecasts for national real and nominal Gross National Product are selected. Econometric equations are then used to forecast Idaho personal income, and further equations then predict tax revenues by major tax category from the personal income estimate. The university forecasters feel that their very aggregated model may be more accurate as a forecasting device than the much more disaggregated model run by the state due to the potential for compounding errors in the state model. The alternative university forecast has been presented to the Select Committee as an objective, outside forecast with no ties to the political system.

Following the hearings, the Committee adopts its own official revenue forecast, which may be higher or lower on particular revenue categories than the executive branch forecast.

Thus the Idaho process is distinguished from that of its western neighbors in several respects. The forecast is annual rather than quarterly. The process is entirely within the executive branch of the government until the hearings conducted by the Select Committee. However, at that point wholly independent forecasts may be presented to the Committee, which is then free to adopt any revenue forecast it sees fit.

Current Forecasts

What do the forecasters currently say about Northwestern economies? The most recent available forecasts at the time of writing are Idaho's December 1984 forecast, Oregon's May 1985 forecast, and Washington's preliminary June forecast. Figure 7 shows personal income in the three states from 1981 to 1984, plus the forecasts for 1985 to 1987. The figure emphasizes the

Figure 7: Personal Income

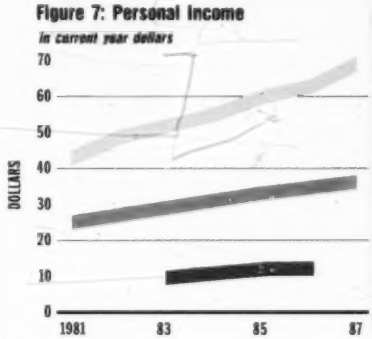


Figure 8: Average Hourly Earnings

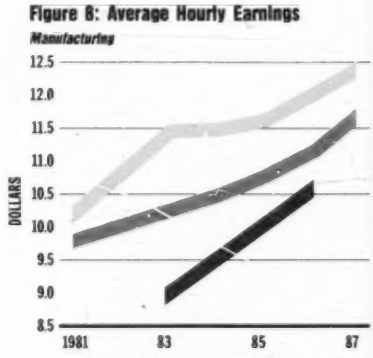


Table 1: Forecasts for Northwestern States Percent Growth, 1985 and 1986

FORECASTED VARIABLE	1985	1986
PERSONAL INCOME		
WA	5.7	5.7
OR	5.9	5.3
ID	6.0	7.3
EMPLOYMENT		
WA	2.7	1.8
OR	3.1	1.7
ID	1.3	1.9
AVERAGE HOURLY EARNINGS		
WA	1.2	1.7
OR	2.2	3.5
ID	5.8	6.4
HOUSING STARTS		
WA	5.6	5.8
OR	6.9	−4.7
ID	0.0	14.8
CONSUMER PRICE INDEX		
WA	3.6	3.9
OR	3.1	4.1
ID	3.7	4.3

relative size of the three states' economies, as well as the pattern of growth. Washington's economy is almost twice the size of Oregon's, while Oregon's is three times the size of Idaho's. All three have been growing at steady but not breathtaking rates following the 1981–82 recession. The growth is expected to continue on through 1986.

The average hourly earnings forecasts (see Figure 8) are especially intriguing because they suggest a convergence of the wage rates in these three states over time. Washington's manufacturing wage is the highest in the region, but it is also growing more slowly than in the other two states. Manufacturing workers in Idaho and Oregon are catching up with Washington workers.

In order to emphasize the contrasts within the region, data on growth rates for five variables are shown in Table 1. The three nominal personal income forecasts range from 5.7 to 6.0 percent growth for 1985, indicating very similar expected rates of growth for this year throughout the region. Idaho's 1986 forecast of 7.3 percent is substantially higher than Oregon's (5.3 percent) or Washington's (5.7 percent) forecast. Idaho's more optimistic forecast may reflect its preparation late in 1984 at a time when the national outlook was more favorable.

The employment forecasts show rather sluggish growth for this key indicator of economic health in all three states. Growth of 1.3 to 3.1 percent is expected in 1985, with a decline in the rate of growth expected in 1986 in Oregon and Washington, and a slight pickup in Idaho.

The average hourly earnings forecasts for manufacturing workers provide evidence of continuing structural change in the Washington economy. While both of its neighbors expect substantial increases in average hourly earnings, Washington forecasts a growth rate of just 1.2 percent in 1985 and 2.5 percent in 1986.

The housing starts forecasts are quite diverse. Washington expects 5.6 percent growth in 1985 and 5.8 percent growth in 1986. Oregon expects faster growth of 6.9 percent in 1985 followed by a sharp decline of –4.7 percent in 1986. In Idaho, no growth is expected in 1985, while the 1986 forecast, consistent with the optimism in the rest of the Idaho forecast, is expected to pick up at a 14.8 percent rate. The reasons for the great divergence on this variable are not apparent.

Little divergence is present in the inflation forecasts, with forecasts ranging from 3.1 to 3.7 percent in 1985, and 3.9 to 4.3 percent in 1986.

These forecasts agree on one important point: none calls for an outright recession in 1986 or 1987. While the precise income, employment, and inflation numbers may vary from one state to another, none of the forecasts places a high probability on an early end to the current economic expansion. Another point of fundamental agreement is on the inflation outlook; no return to high rates of inflation is foreseen for the region unless the pessimistic scenario discussed below is realized.

Decision Making and Policy Uses of Forecasts

For forecasts to be useful to anyone, decision makers in the public and private sectors must act on the basis of information obtained from the forecasts. There is considerable evidence that the state economic and revenue forecasts are used by public and private decision makers. Of course, the state governments which prepare the forecasts are the principal users. In each of the three states, the revenue forecast is an important input to the budgetary process. By setting a spending limit based on anticipated revenues, the forecast determines the overall level of the state budget, and the need for a change in tax rates. Forecasts have been cited time and time again as the basis for management actions by state executives, particularly during recessionary times when the forecasts provide a guide as to the extent of service cutbacks or temporary tax increases needed to maintain the fiscal condition of the state. Private decision makers may also use the economic forecasts as a check on their own forecasts, or as their only guide to the level of economic activity in these states.

Readers who would like to obtain copies of the forecasts reviewed in this article may do so by writing to the following:

Division of Financial Management
State of Idaho
Statehouse Room 122
Boise, ID 83720
$15 per year

Executive Department
Budget and Management Division
State of Oregon
155 Cottage Street NE
Salem, OR 97310
$5 per copy

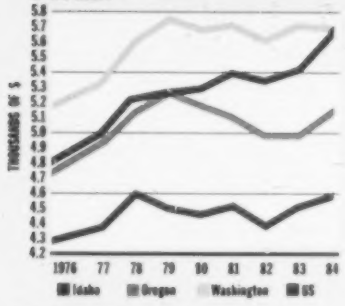
Office of the Forecast Council
State of Washington
Evergreen Plaza Building, AX-02
Olympia, WA 98504
No charge

One useful step in the forecasting process would be to add alternative revenue forecasts to the process in conjunction with the alternative economic forecasts already included in the Oregon and Washington efforts. Using control, pessimistic, and optimistic scenarios from the national forecasts, both of these states prepare alternative state economic forecasts. However, revenue forecasts based on the pessimistic and optimistic economic scenarios are not currently presented. In previous years, alternative revenue forecasts have sometimes been presented in the Washington forecasts. Otto Eckstein, late dean of American forecasters and founder of the DRI model of the U.S. economy, has said: "It must be recognized that much error remains in the forecasts, enough to preserve considerable humility *and to be a warning to users against acting on unique valued projections.*" Adding pessimistic and optimistic revenue projections would help state executives to understand the risks they run by including too little or too much in contingency funds, and in evaluating the sagacity of budget and revenue decisions.

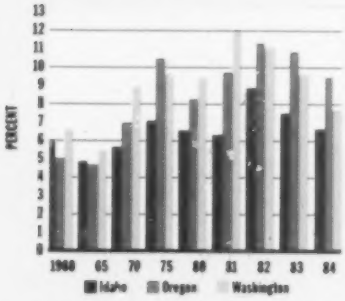
Pacific Northwest Annual Economic Indicators

REAL PERSONAL INCOME PER CAPITA

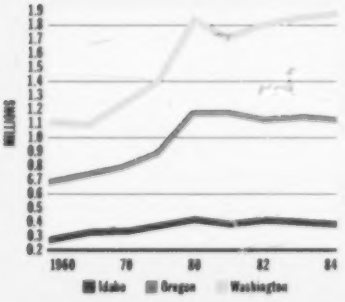
In 1972 dollars



UNEMPLOYMENT RATE



EMPLOYMENT



POPULATION[A,I]

In thousands

YEAR	ID	OR	WA
1960	667	1769	2853
1965	686	1937	2967
1970	713	2091	3409
1975	832	2338	3621
1980	944	2633	4132
1981	964	2669	4235
1982	977	2668	4276
1983	987	2658	4302
1984	1001	2674	4349

PERSONAL[B] INCOME

In millions $

ID	OR	WA
1236	3930	6772
1679	5329	8867
2378	7795	13827
4360	13305	22484
7679	24553	42541
8626	26528	47664
8805	27078	50004
9450	28585	52368
10181	30974	55344

FARM INCOME[D]

In millions $

ID	OR	WA
159	185	268
8867	238	186
274	227	356
434	390	866
518	540	858
605	542	1089
417	471	1056
492	493	1153
528	446	972

IMPLICIT[B] PRICE DEFLATOR

for personal consumption 1972=100

YEAR	
1960	71.9
1965	77.2
1970	92.5
1975	125.2
1980	179.0
1981	194.5
1982	206.0
1983	213.6
1984	220.4

UNEMPLOYMENT[C] RATE

percent of labor force

ID	OR	WA
6.0	4.9	6.4
4.8	4.6	5.4
5.8	7.1	9.2
7.3	10.6	9.5
6.5	8.3	7.9
6.3	9.9	9.5
8.7	11.5	12.1
7.4	10.8	11.2
6.3	9.4	9.5

TOTAL[C] EMPLOYMENT

In thousands

ID	OR	WA
264	682	1020
267	776	1107
281	803	1285
342	929	1412
404	1188	1828
401	1205	1806
388	1171	1779
396	1196	1838
402	1210	1859

WAGE & SALARY[C] EMPLOYMENT

In thousands

YEAR	ID	OR	WA
1960	155.2	509.2	812.6
1965	177.6	607.4	896.6
1970	209.3	709.2	1080.0
1975	273.0	837.4	1225.7
1980	330.9	1044.6	1608.3
1981	327.8	1018.4	1612.0
1982	312.2	960.8	1569.2
1983	317.9	966.7	1585.1
1984	325.9	1004.0	1640.4

AEROSPACE[C] EMPLOYMENT

In thousands

WA
57.8
57.0
61.5
50.4
79.6
79.0
75.0
64.9
66.7

LUMBER AND[C] WOOD PRODUCTS EMPLOYMENT

In thousands

OR	WA
71.9	44.4
74.2	46.9
66.8	42.2
69.6	47.2
59.5	47.0
63.8	44.4
55.6	39.0
62.6	42.1
66.0	40.6

PAPER[C] EMPLOYMENT

In thousands

WA
18.0
19.8
19.8
16.4
17.6
17.2
16.2
15.8
16.1

CONSTRUCTION[C] EMPLOYMENT

In thousands

YEAR	ID	OR	WA
1960	9.6	26.1	44.6
1965	11.4	33.4	46.4
1970	10.9	29.5	53.3
1975	16.1	35.3	59.5
1980	15.8	46.5	92.6
1981	16.7	37.5	90.3
1982	13.8	28.9	75.6
1983	13.1	27.0	73.6
1984	13.2	29.9	76.6

MANUFACTURING[C] EMPLOYMENT

In thousands

ID	OR	WA
28.9	144.4	216.6
33.3	158.2	227.0
40.4	172.3	239.4
47.8	182.1	244.0
53.3	215.1	308.7
52.7	202.7	303.3
47.8	185.7	289.9
50.3	188.8	277.9
54.1	198.7	284.8

SOURCES:
A. Bureau of the Census, U.S. Department of Commerce.
B. Bureau of Economic Analysis, U.S. Department of Commerce
C. State of Idaho Department of Employment.
State of Oregon Employment Division.
Washington State Employment Security Department.
D. F.W. Dodge Division, McGraw-Hill Information Systems Co.
E. Western Wood Products Association.
F. American Plywood Association.
G. "Pulp, Paper, and Board," Bureau of the Census.
H. U.S. Forest Service.
I. Direct Service Industries, Inc.
J. Pacific Northwest Utilities Conference Committee.
K. Bonneville Power Administration.
L. Bureau of Labor Statistics, U.S. Department of Labor.

FOOTNOTES:
1. Includes armed forces residing in each state. 1965, 1975, 1981-1984 are July 1 estimates.
2. Index of the deflated value of construction contracts.
3. 1000 mill evaluations, coast region (Oregon and Washington), census basis.
4. Although 1960 is not available, the figure for log exports in 1961 is 5330 million.
5. Data do not account for export of aircraft or shipments that pass through the Northwest and clear customs elsewhere. 1960 figures do not include exports or exports by air.
6. Figures includes six primary aluminum producers in Washington, Oregon, Idaho, and Montana.
7. CPI for all urban consumers.
8. One mill = 0.1 cents. Price cited is wholesale BPA price to publicly owned and investor owned utilities for service to residential customers. From 1938 to 1965, the rate was 2.75 mills, but increased Dec. 20, 1965 to 3.25. On July 1, 1981, the rate increased from 7.26 to 11.7. On Oct. 1, 1982, the rate increased to 18. On Oct. 1, 1983, the rate increased to 22 mills per KWH.

CONSTRUCTION[D] CONTRACTS
In millions $

YEAR	ID	OR	WA
1960	115.4	364.6	632.3
1965	186.8	585.7	1006.7
1970	197.4	634.3	1478.2
1975	398.6	1035.9	2019.3
1980	634.5	1926.1	4795.1
1981	721.9	2038.2	3587.9
1982	508.4	1379.9	3394.8
1983	544.8	1414.7	3667.8
1984	633.7	1781.9	3848.8

BUILDING[D2] INDEX
1972 = 100

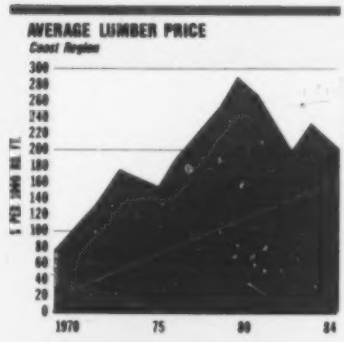
ID	OR	WA
57.0	55.5	60.5
90.2	87.2	94.2
73.9	73.2	107.3
153.6	77.3	94.7
107.4	88.3	138.2
68.8	85.0	94.0
65.8	55.1	85.2
71.0	56.8	92.6
80.0	69.4	94.2

AVERAGE[E3] LUMBER PRICE
1000 board ft.

75.01
76.09
91.88
154.63
267.59
232.49
198.43
228.88
215.01

PLYWOOD[F] PRODUCTION
In million board ft.

WA & OR
6535
9720
8663
7722
6786
6215
5700
8141
8319



LUMBER[E] PRODUCTION
In million board ft.

YEAR	OR	WA
1960	7402	3377
1965	7580	3648
1970	9680	3189
1975	6342	3104
1980	5784	3161
1981	5115	3243
1982	4682	3059
1983	6579	3821
1984	6772 est	3933 est

WOOD PULP[G] PRODUCTION
In thousand short tons

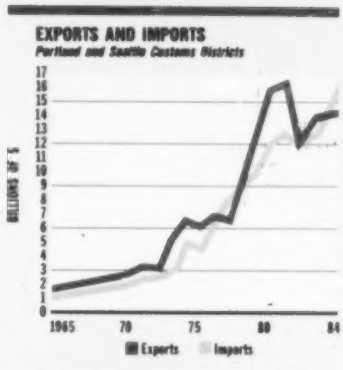
WA	OR
NA	NA
NA	NA
3848	2843
3585	2480
3519	3787
3274	2489
3394	2656
3758	2845
NA	NA

LOG[H] EXPORTS
In million bd. ft.

WA & OR
NA
901
2216
2225
2632
1987
2568
2592
2722

EXPORTS IMPORTS
Portland and Seattle Customs Districts
In millions $

EXPORTS	IMPORTS
625	305
829	427
2688	1651
6224	4781
15770	11836
16155	12787
12208	11899
13723	12826
14216	16323



ALUMINUM[I,6] PRODUCTION PNW
net primary ingot (tons)

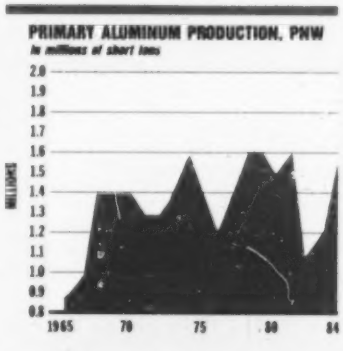
YEAR	
1960	527200
1965	796500
1970	1390800
1975	1411000
1980	1547439
1981	1600062
1982	1135680
1983	1174791
1984	1574337

ELECTRICITY[J] PRODUCTION PNW
In millions of KWH

69386
99873
143993
171797
206221
195060
184822
181405
195197

BPA ENERGY SALES[K]
In millions of KWH

25449
37211
56327
68934
72448
82001
81381
82781
87932



CONSUMER PRICE INDEX[L7]
Portland Seattle-Everett
1967 = 100

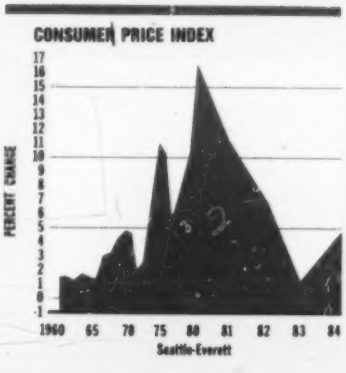
YEAR	PORTLAND	SEATTLE-EVERETT
1960	87.1	87.9
1965	94.6	94.5
1970	113.2	114.0
1975	156.5	155.8
1980	255.4	252.1
1981	278.2	279.7
1982	287.0	297.8
1983	290.1	302.8
1984	301.0	313.9

AVERAGE PRICE[K8] OF BPA POWER SALES
mills per KWH

2.78
2.78
3.25
3.51
7.26
11.7
18
22
22

AVERAGE[C] HOURLY EARNINGS
for manufacturing employees

ID	OR	WA
$2.25	$2.55	$2.63
2.65	2.94	2.98
3.29	3.82	4.06
4.77	5.53	5.82
7.55	8.65	9.64
8.04	9.47	10.59
8.62	10.02	11.17
8.49	10.21	11.42
9.34	10.44	11.61



BPA: Options for the Direct Service Industries

The aluminum industry, attracted to the Pacific Northwest in the 1940s by cheap electric power, is in trouble. In the past ten years energy costs in this region have soared, while aluminum markets have become less predictable and more competitive. Today the aluminum industry in the Pacific Northwest is only marginally profitable, and some of the smelters are losing money. Faced with intensive price competition from lower cost plants elsewhere, the aluminum industry is at a crossroads. At stake are 9,000 direct jobs in the Pacific Northwest, and up to 20,000 indirectly.

Bonneville Power Administration (BPA), which sells power directly to these aluminum plants, is under pressure to find additional sources of revenue to meet its rising costs. Raising the rates to these "Direct Service Industries" (DSIs) would quite likely drive them out of business, while lowering rates to make the DSIs competitive would force other BPA customers to pick up the bill. Caught between the proverbial rock and a hard place, BPA has undertaken an assessment of how various rate alternatives will affect the DSIs and its other customers. This assessment is called the "DSI Options Study."

What are BPA's options? How will BPA's chosen course affect utilities and their ratepayers? Are there options which meet BPA's goals but which are not included in the options study BPA has undertaken?

Structural Change in the Aluminum Industry

To understand the present dilemma, some features of the world market for aluminum need to be sketched. Aluminum ingot, the major product produced by the aluminum companies in the Northwest, is a completely homogenous product. This means that one ingot is the same as any other, and buyers are indifferent to the country of origin. They are only interested in obtaining the best possible price.

Capital costs for the Pacific Northwest plants are quite low, since the major investments were made decades ago. Once major plant investments are made, capital costs are "sunk" and operating decisions are made with an eye to recovering variable costs, as well as to any profit opportunity that can be used to amortize sunk costs or return a dividend to stockholders. This low current capital cost gives these plants an advantage that allows them to keep competing despite higher energy costs.

The variable costs of the industry are approximated by the following percentages:

	World Average	PNW Average
Alumina	39.9%	28.2%
Energy	29.0%	32.1%
Labor	17.0%	16.7%
Other	14.1%	23.0%

Labor costs differ from one location to another, but are the smallest of the three major variable cost factors. "Other" costs include transportation costs, which are high in the Pacific Northwest because we are far from major markets. Electricity costs are a major cost item, and these costs vary greatly among the producing countries with a range from 5 to 75 mills per kWh. Electricity costs are the only cost factor which can be affected significantly by the choice of plant location.

Six countries or regions are the major producers: Australia, Brazil, Canada, Japan, the United States, and Western Europe. The so-called "ABC countries," Australia, Brazil, and Canada, all have very low cost power for the aluminum industry. In Brazil and Canada, this power is produced by hydroelectric systems, just as in the Northwestern United States, while in Australia the power comes from low cost coal-fired systems. Japan's plants are oil-fired and are so expensive to operate that the country has made a conscious decision to shut down its aluminum smelting industry.

The smelters in the Pacific Northwest used to enjoy low cost hydropower as well, and this advantage combined with sunk plant costs provided a very competitive, low cost segment of the worldwide industry. However, the rate increases the DSIs have faced in the past ten years leave the Pacific Northwest near the high end of the supply curve. The region's aluminum smelters now are "swing plants" which go in or out of production depending on demand.

Unfortunately, the other structural change in the market has been from a regime of stable growth at 9.5 percent per year in the postwar era to an unstable, highly cyclical regime with a much lower aggregate growth rate in the 1970s and 1980s. The instability is the result of fluctuations in energy markets, greater use of scrap metal, and the establishment of futures markets. Consequently, the "swing plant" status has meant that the Northwestern smelters are frequently shut down.

The Options Study

The long-term issue for aluminum smelting in the Northwest is whether the plants can remain viable at all or whether, like the Japanese plants, they are slowly becoming extinct. In that context, the DSI Options Study addresses rate-making alternatives for the DSIs which may provide some short- to medium-term benefits to the industry and to others in the Northwest. However, the question of long-term viability is still very much open.

Faced with both a surplus of energy over the next ten to fifteen years and a troubled customer group which buys a quarter to a third of its total supply, BPA is seeking a way to sell more energy to the aluminum companies, thereby resolving its own problem, while also contributing to the short- to medium-term viability of this important industry. The following alternatives are addressed in the study:

1. Increased interruptibility of DSI loads. A quarter of the DSI load is now interruptible, allowing the BPA to count this load as part of its reserves. In this option, a substantially higher proportion of the DSI load would be made interruptible and sold to the DSIs at a lower rate. The lower rate might keep some smelters in operation, generating more revenues for BPA relative to a "no action" scenario, while also creating reserves which would allow more firm power to be offered to other customers, perhaps in California. The increased BPA revenue from these sales would reduce revenue requirements for other customer classes.

2. Modernization/conservation. This option would involve BPA contributions to the aluminum companies to pay for moderni-

zation and conservation investments at the smelters. The goal would be to achieve lower production costs, thereby making the plants more competitive.

3. Long-term variable rates. This option would tie the BPA power rate to the price of aluminum, somewhat analogous to the current policy of offering a short-term discount to the aluminum companies.

4. Service from other power suppliers. If BPA permitted the DSI plants to buy power from low cost Canadian suppliers, one of the advantages of Canadian aluminum plants would be minimized and the competitiveness of the Northwestern plants would be enhanced.

BPA's preliminary analysis of the costs and benefits of these options for both the DSIs and the utilities which buy power from the BPA suggests a number of conclusions:

Taking no action at all would result in a declining aluminum industry, one that would shrink to between one-third and three-fourths of its present capacity by the year 2015. This is the "base case" against which the other alternatives are evaluated. The base case assumes that BPA does not institute a customer charge on DSIs, but continues its current incentive rate; that the DSI contract is renewed in the year 2001; and that the real price of aluminum is fixed at 81 cents/lb. for the remainder of the century.

The **increased interruptibility** option would keep one or two of the highest cost plants in operation to the end of the century instead of closing them soon. Thereby, employment benefits of 900 to 1500 aluminum plant jobs would be maintained. In addition, firming up additional capacity and selling it out of the region would create some benefits to other BPA customers after the year 2000.

The **modernization/conservation** option would affect one to ten smelters, with benefits of 700 to 2000 jobs. No benefits would be created for other BPA customers.

Establishing a **long-term variable rate** would do very little for the industry. Compared to the no action case, a variable rate would maintain no more than 160 jobs, and in some cases actually contribute to a decline of over 1300 jobs. This option would do nothing for other customers. While this option has been featured in many media discussions of the options study, it does not seem to be a preferred alternative.

Allowing the aluminum companies to obtain **service from other suppliers** of electric power has not yet been evaluated, but will be as the options study continues. This option may have the potential for keeping the aluminum industry in the region in the long run, but will raise difficult issues for BPA vis-a-vis other customers who would like access to lower cost resources.

Reactions to Options Study

BPA faces fixed revenue requirements which are likely to increase still more in the future. BPA does not have the option of avoiding payments on the WPPSS plants it financed, nor can it any longer avoid payments to the federal government on the dams and transmission system that are the backbone of the BPA electric power system. Indeed, it faces the prospect of congressional or administrative action to change the terms on that debt to the federal treasury. While the threat to make BPA pay market interest rates on a fixed repayment schedule has been averted for the moment, it is not likely that the issue will go away. BPA will need increased revenues to cover any change in the repayment schedule or interest rates.

In this context, any policy which reduces power rates for one class of customers must necessarily raise rates to other customer classes by the amount of the discount, less any increased power consumption by the beneficiaries of the discount. Since the whole point of the DSI Options Study is to find the option with the greatest benefit to BPA and all of its customers, this is not a simple zero sum game. Relative to the base case of a declining aluminum industry, some options can result in benefits to all customers. Benefits can result from increased consumption by the aluminum companies, which reduces the revenue requirements which other customers must cover, and from increased out-of-region sales made possible by firming up more of BPA's current surplus.

However, some of the costs of the DSI "discounts" are going to be passed on to other ratepayers—ratepayers who have faced a series of BPA rate increases over the last ten years. These ratepayers react to the change from current rates, not to the nebulous concept of higher rates that would have to be paid in the base case scenario. Convincing the publicly and privately owned utilities, and the irrigation customers of BPA, that they should contribute to the health of the aluminum companies through higher rates is not going to be easy.

For those communities with smelters in their immediate vicinity, rate increases associated with a DSI option may be easier to accept. Local ratepayers will be directly affected by the viability of the local smelter and may be inclined to accept marginally higher power rates to keep a local industry running. For others with no nearby smelters, the higher rates will be much more difficult to sell.

The policy choice would be easier if there were ideas on the table on how to keep the smelters going indefinitely. However, the hard reality is that the "ABC countries" seem likely to remain the least cost producers well into the next century. And in contrast to our government, the Western European governments stand ready to subsidize their industry to keep it alive. The Pacific Northwest is faced with making the best use of a regional power surplus while planning for the slow decline of one of its basic industries over the next two decades.

The decline seems to be unavoidable, so the real issue may be to make the best deal we can for disposition of BPA's surplus. Peter Johnson, BPA Administrator, stated at the recent BPA/League of Women Voters Symposium that the goal of the DSI Options Study was *not* to find a way to keep the DSIs in business, but *to make the best possible decision for BPA and its many ratepayers.* If the best deal involves some discounts to aluminum companies, so be it, but such deals need to be predicated on a clear picture of costs and benefits to other BPA customers.

If the real policy issue is disposition of the suplus, a wider "options study" is needed to look at other ways of using the surplus. Sales to California are often mentioned but seldom consummated. Other options may exist. Cutting one's prices is a time-honored and economically valid way of dealing with a surplus. The consequences of such a policy would depend on the regional elasticity of power demand, and on BPA's flexibility in dealing with its sunk capital costs. How about using the surplus to attract new industry into the region? Grant County, with its two county-owned hydroelectric projects, is having some success in attracting electricity- and labor-intensive industrial customers into its service territory by pointing out the low costs of its power supplies to potential investors. Such options need to be compared with the DSI options if the region is to benefit to the greatest degree from the current BPA surplus.

A copy of the "DSI Options Study" (DOE/BP-423) may be obtained from the BPA, P.O. Box 12999, Portland, OR 97212.

Taxes and New Business in Washington

by Stephen A. Duzan

The Washington State Legislature has adjourned its 1985 regular session. As this is written, a special session is anticipated at which lawmakers will reattempt to pass a budget for the 1985–1987 biennium. However, because the special session will be limited to fiscal matters, it is possible to begin to evaluate the regular session (and the political season which preceded it) concerning economic development matters.

The term "economic development" is used here in its broadest sense. It includes public and private activities designed to stimulate both new business formation and the attraction of outside established firms seeking to expand or relocate facilities or operations. Viewed in this way, there has never been a cohesive plan for economic development in Washington state. There have been fragmented, often uncoordinated, sometimes conflicting efforts which addressed one element or another of the problem. These have concentrated almost exclusively on luring businesses to locate facilities here.

Economic development should, however, encompass improvement of the whole of the internal business environment, involving many social and economic areas. Of particular importance are state and local taxation policies; state and local regulatory activities; land use planning, zoning, and the permit process for plant siting; quality public school education; quality of higher education, particularly engineering and technological research programs; quality of lifestyle, including preservation and protection of the environment; availability of adequately trained (or trainable) workers, particularly middle and senior management talent; and availability of capital.

Clearly, not all of these are, or should be, the responsibility of government. In recent years, however, it has become clear that direct stimulation and promotion of business development are primarily the domain of state and local governments rather than the federal government. These governments have created a wide range of inducements which are perceived to make one location or another more attractive. Tax deferral or forgiveness, low interest loans backed by revenue bonds, incubator facilities, free or extremely cheap land, subsidized training programs, and so on, are now routinely available to "attractive" (meaning clean, low energy consuming, job creating) companies.

The state of Washington has not been a leader in the economic development sweepstakes, in either innovation or achievement. In some respects, its state and local governments have found many of the established "inducements" foreclosed to them by the state constitution's prohibition on the lending of public credit. This has made illegal such concepts as free incubator facilities, specialized tax breaks, free land, or land

Is the tax structure in Washington more of a burden on a new business than the tax structure in other states? Stephen Duzan of Immunex Corporation says yes. He describes what one group of concerned business people tried to do about it.

development at government expense.

Also, Washington's economy has always been resource-based. Timber, agriculture, fishing, and mineral interests have held great power since territorial days. None of these are steeped in innovative economic development tradition. Support for "costly" programs to encourage new industries has not been viewed sympathetically by the more established ones.

An additional factor is Washington's populist political tradition. Perhaps more than any other state, Washington has viewed business with skepticism. Proposals designed to facilitate growth and diversification must overcome the virtually certain suspicion that they represent a ripoff—an unnecessary

concession designed to feather a few pockets at the expense of "the little man," the ordinary taxpayer.

By the beginning of this decade, one could sense a change in attitude about the need to enhance Washington's economic development. This is, in part, reflective of national trends. The fashionableness of an economic development role for states and cities is an element. In addition, Washington shares in the general national decline of traditional industries. The severity of the 1980–81 recession raised concerns among many who take jobs and economic vitality for granted. Entrepreneurship and small business have achieved greater favor. In addition, there is a diminished belief that government can unilaterally solve society's social and economic problems, with a resultant increase in the expectation that the private sector must play an increased role.

The change in attitude in Washington is also prompted by some circumstances peculiar to this state:

- Rapidly rising electrical rates threaten important industries, such as aluminum smelting.
- Washington's resource-based economy usually feels recession sooner, longer, and more severely than other areas. The state was extremely hard hit in the 1980–81 recession, and has not fully participated in the subsequent national recovery. The level of unemployment in the last decade has been above the national average.
- State government has experienced repeated budget woes and has imposed tax surcharges and increases. This is due partly to social problems occasioned by economic ones; partly to court-mandated state funding of basic education; partly to the citizens, who have voted to eliminate three tax sources (the sales tax on food, the sales tax on the value of trade-ins, and the inheritance tax); and partly to an inability of government to curb spending increases.
- Public confidence has been eroded by the general economic malaise and by the WPPSS debacle.

As is perhaps predictable, this climate has produced a cacophony of voices, proposals, and programs. By 1984, several economic development thrusts were in evidence. Many cities and counties had established or were considering economic development commissions, industrial development corporations with the power to issue revenue bonds for backing loans to private projects, and the like. Regional or county economic development councils, established and supported by the private sector, were in place to recruit firms to their areas. A private statewide entity with the same objective was being launched.

The legislature created the Small Business Improvement Council (SBIC), an entity with a nearly unlimited charter to examine the activities of state government to determine their impact on the formation and operation of smaller and emerging businesses. The initial members of this council were appointed in July 1984 by Governor Spellman. The legislature also created and authorized initial funding for a Washington Technology Center, to be a focal point for high-technology research and development.

In the private sector, the Washington Council for Technology Advancement was established. Membership in this group is comprised of leading technology companies, large and small. It chose, as its primary focus, the funding of research and training at the University of Washington and Washington State University. The Washington Roundtable, an organization of the chief executive officers of the state's largest companies, undertook to study and propose improvements for K–12 public education.

Out on the political stump, politicians were, almost without exception, converts to the cause of economic development. As could be expected, campaign rhetoric was long on generality and short on detail, but most candidates for governor and the legislature were for programs to aid job creation through business expansion and for elimination of anything which impeded this goal.

As the 1985 legislative session began, the prospects for improvement in key areas were reasonably bright. In the end, the session produced almost nothing tangible. There were only two positive results of significance. The Department of Commerce and Economic Development was reorganized and its funding was increased. Salaries for University of Washington and Washington State University faculties were increased by percentages greater than for other state employees, suggesting an understanding of the critical role of quality higher education

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Stephen Duzan is president and chief executive officer of Immunex Corporation. In 1984 he was appointed to the Small Business Improvement Council of the state of Washington, on which he serves as co-chair of the task force on taxation and business climate.

in economic development. Both of these positive results are potentially vulnerable during the upcoming special session.

Two backward steps probably also occurred, although the special session could restore these. The Washington Technology Center will likely receive only a small portion of its requested funds, leaving it substantially behind comparable entities in other states. The SBIC will probably not be funded at all.

What went wrong? How did the glow of 1984 dissolve into the inertia of 1985? It is instructive to look at one part of the story, the efforts of the Small Business Improvement Council in the taxation area, in order to understand the great distance which Washington must yet cover to put its economic development house in better order.

The SBIC is comprised of heads of smaller businesses, leaders of business organizations such as Chambers of Commerce, and representatives of state agencies which interact with businesses. At its initial meeting in August 1984 it divided itself into three task forces: taxation and business climate, business services and coordination, and regulation. The latter two were viewed as areas requiring longer-range studies before substantial proposals were prepared. The first was expected to move more rapidly.

The taxation task force retained the accounting firm of Peat, Marwick, Mitchell and Co. to prepare a report on the impact of Washington state taxes on new business creation. In order to achieve a useful report, and in consideration of perceived political realities, the task force established several guidelines for the study:

- A widespread perception existed that the state's tax structure is extremely unfair to new companies. The study was, therefore, to be quite specific. It would measure the degree to which such firms were penalized, from a taxing standpoint, if any, by their decision to locate in Washington. The study would concentrate on the "start-up" period, the duration of which was recognized to vary widely, primarily by industry.
- There had previously been many theoretical studies of the Washington tax structure. This study would be practical, utilizing data from actual companies.
- Peat, Marwick was expected to propose and defend recommendations to alleviate any problems identified.
- The task force did not believe it politically feasible or within its charter to undertake general reform of business taxation. Therefore, if findings supported the contention that the smaller firms were unfairly penalized by the tax code, the task force wished to mitigate or eliminate the penalties, not rewrite the whole code.

Peat, Marwick studied the tax impact for twenty-eight companies based on actual financial data for their start-up periods. The firms, which were guaranteed anonymity, were selected to illustrate sixteen particular industries identified by the task force as important to the economic future of Washington. These included high-tech companies as well as more traditional firms. All firms had between 5 and 500 employees, with a majority having fewer than 50. They were geographically spread throughout Washington. Some out-of-state firms were also included. The study was intended to be illustrative and was not a scientific sampling.

Taxes were separately calculated for the twenty-eight firms as though each were located in fifteen different states and the province of British Columbia. Relative tax impact for these separate jurisdictions was then compared. Besides Washington, the list included Arizona, California, Colorado, Georgia, Idaho, Illinois, Massachusetts, Michigan, Minnesota, Nevada, New Mexico, North Carolina, Oregon, Texas, and British Columbia. States were selected based on the frequency with which Washington competes with them to attract new industry.

The study was limited, as was appropriate for each state, to the combination of business and occupation, income, sales, property, and franchise taxes. These were selected because they are imposed on the property and profits of new and expanding businesses. Except for sales and property taxes, local taxation was not included, both to simplify the study and because it was not felt to be significant. Payroll taxes were likewise not included.

The Peat, Marwick report concluded that " . . . the total tax load on the new and expanding businesses studied was generally higher in Washington than in competing states." Washington's tax load " . . . was the highest for sixteen of the twenty-eight companies and was among the three highest for twenty-two of the twenty-eight firms."

Peat, Marwick made four specific recommendations:

1. Business and occupation taxes for new businesses which experience a loss during their first few years of operation should be forgiven.
2. No sales tax should be charged on labor used to construct or make tenants improvements to commercial buildings.
3. As an alternative to recommendation two, relevant sales taxes could be deferred.
4. No sales tax should be charged on purchases and rentals of manufacturing equipment, R&D equipment and molds, and tools and dies.

Peat, Marwick found that real property taxes did not contribute to the more detrimental picture in Washington, and made no recommendations with respect to it.

Peat, Marwick also stated that their proposals could be modified to target the relief to specific businesses and to reduce the impact on state revenues. For example, ceilings could be imposed to insure that benefits were directed at similar businesses. Job creation requirements could be imposed. Benefits could be limited to firms in "base industries," defined as firms " . . . which do not primarily serve Washington businesses or their employees." Finally, recommendations one and four could be changed to deferrals.

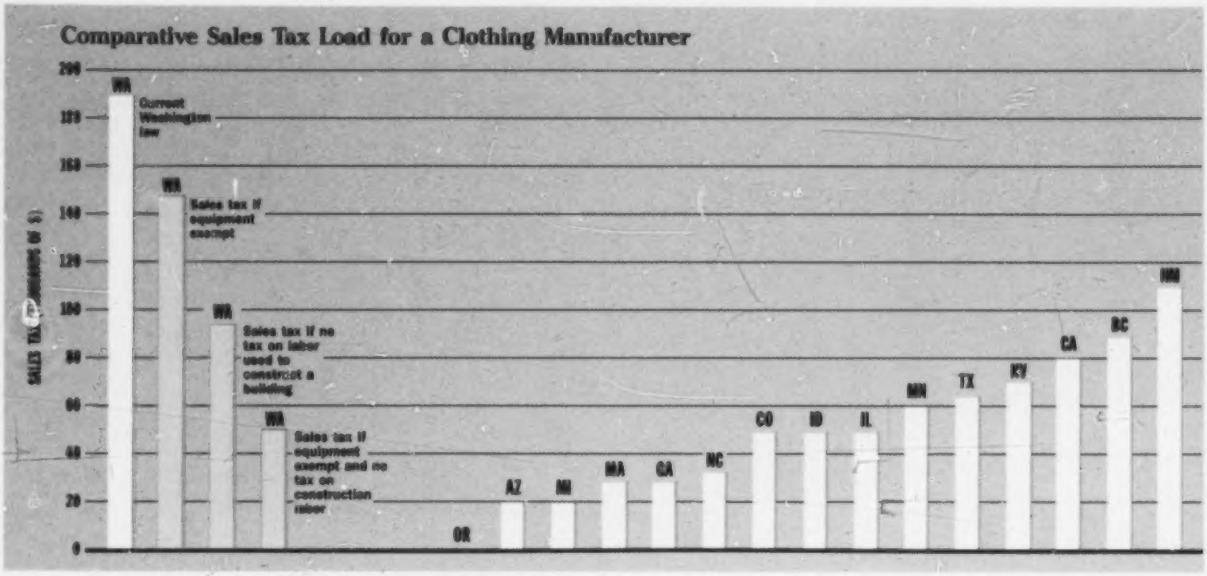
The SBIC task force concluded that Washington's tax structure was detrimental to start-up businesses and that tax loads made competition extremely difficult for firms trading outside the state. It also found that the state's tax structure made recruitment of outside firms more difficult.

The study showed that Washington's sales tax is a greater problem than is often realized. The figure on the next page offers a typical example from the Peat, Marwick report. It shows the comparative sales tax load for a clothing manufacturer.

Not only did Washington have the highest sales tax, but it also had the highest sales tax rate of all the states studied, except Illinois. Moreover, nine of the fifteen competing jurisdictions either exempt or give some type of preferential treatment to sales taxes on manufacturing equipment. In addition, Washington was alone in applying sales taxes to the labor used to construct facilities.

The study also showed that the business and occupation (B&O) tax was detrimental to many types of new businesses, particularly those with longer start-up periods. Because the B&O tax is assessed on gross revenues without regard to profitability, newer firms often find themselves paying taxes, even as they lose substantial sums.

Taken as a whole, the SBIC believed it had a very compelling case. As is well known,



newer, smaller businesses are the job creators, yet Washington's tax structure falls much harder on most start-ups than is the case in comparable states. Clearly, it seemed, the state government should be eager to improve this situation in the interest of job creation and economic vitality.

The task force proposed four bills to the 1985 legislature. These were designed to accomplish the following:

1. Exempt manufacturing equipment, computer software, and R&D equipment from all sales tax.
2. Defer payment of sales taxes levied on the construction of new facilities for three years.
3. Defer payment of B&O taxes by firms which lose money in their initial three years after start-up.
4. Reduce the B&O tax rate on research and development revenues from the professional rate (1.5 percent) to the general manufacturing rate (.484 percent).

With a realistic set of ceilings on amounts which could be deferred or forgiven, and with appropriate job creation requirements, the Department of Revenue estimated the total reduction in revenue which would result from these measures at $59 million. Of this amount, $34 million would be deferred, and ultimately collectable by the state. Governor Gardner proposed his own version of sales tax deferral, which applied to both construction of facilities and purchase or rental of equipment.

In the end, all SBIC proposals died. None of them was even accorded a hearing in the House of Representatives. They were heard in the Senate only by the Sub-Committee on Small Business. They were never seriously considered by the legislative leadership, and were not pushed by Governor Gardner.

The Governor's own sales tax deferral bill was passed and signed into law. It was amended so as to be available only to firms locating in a "distressed county," one in which unemployment exceeds the statewide average by 20 percent or more. Firms locating in King, Pierce, Snohomish, Spokane, or Clark Counties will not be eligible, meaning that most new business activity will not be benefited. *(Editor's note: A second sales tax deferral bill was passed in the June special session giving a three-year deferral on construction and equipment costs with a five-year payback. It will be available only to out-of-state manufacturing companies without regard to their county of location. In-state firms are not eligible.)*

It would be easy to write off these results to the revenue woes which ensnarled and stalemated the 1985 legislature. But, while this clearly affected the climate, it was not the whole story. The bills were almost certainly doomed from several standpoints. They were ignored by the leadership of the House Ways and Means Committee which had its own agenda—a "value added tax" designed to replace the B&O. The SBIC, comprised of private citizens, had no effective means to lobby for its own proposals. It had no charter to propose new revenue sources to replace those it proposed cutting. Tax change appears to be possible only if it is largely revenue neutral. The support by many elected officials for improvements in the business climate appears to be lacking in substance. The failure of the SBIC to achieve its goals is typical of the outcome of most economic development proposals in Olympia this past winter.

One is left to conclude that it may be impossible to expect the legislature and the governor to take the broad, bold steps necessary to seriously embark on a cohesive, wide-ranging economic development plan. Too much of their time and energy must, of necessity, be spent on nearer term objectives. What is needed is longer-range thinking, and that is not the stuff of legislative bodies—Washington's or any other.

The development of a blueprint for economic development may require a private citizen's effort of greater magnitude. The initial stirrings of such a movement can now be heard in the state. An effort of this type might examine and offer proposals across the spectrum of the issues involved: taxation, fiscal policy, education, regulation, land use, and so on. It has not gone unnoticed that Washington's centennial will occur in 1988, and that development of an outline for its economic future might be an appropriate commemoration. Clearly, based on the SBIC experience, tackling hard problems like taxation in an isolated way will not lead to much success.

Comparable Worth in the

The argument over equal pay for comparable work is heating against the comparable worth concept, and a labor union

Against

Association of Washington Business

The concept of "comparable worth" has been termed by some feminists as "the women's issue of the eighties" and called "the looniest idea since Looney Tunes" by the chair of the U.S. Civil Rights Commission. Whatever the label, it is a concept that is getting much attention from the media and is being studied in many states around the country.

What does comparable worth mean? Simply stated, comparable worth refers to the theory that every job has a worth to an employer or society that can be measured and assigned a numerical value. The concept of comparable worth is commonly referred to by proponents as being synonymous with pay equity. It is not pay equity; it's a different matter altogether.

The concept of comparable worth must be distinguished from the widely accepted legal requirement that an employer must pay equal wages to men and women who do the same work. This requirement, set forth in the federal Equity Pay Act as well as in many state statutes, is known as "equal pay for equal work" and does not require courts or enforcement agencies to engage in determinations as to the relative "worth" of different jobs. When Congress drafted and

(continued on page 22)

The Association of Washington Business is an industry group which takes an interest in public policy issues.

Private Sector: A Debate

up in the private sector. A group of business people argues representative picks up the debate in favor of the issue.

FRED BIRCHMAN

In Favor

Karen Place, I.F.P.T.E., AFL-CIO

The controversy over "comparable worth" is an exceptionally confusing one, where the real issues disappear behind thickets of irrelevancies. Perhaps the term comparable worth itself is part of the reason.

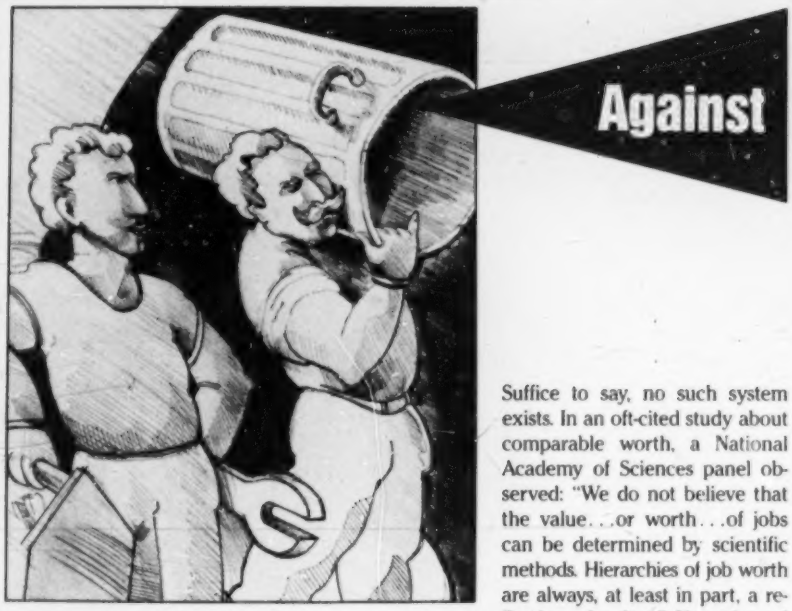
I am *not* an advocate of any compensation policy which could accurately be described as "equal pay for jobs of comparable worth." I do advocate pay equity for sex-segregated jobs—or more explicitly, higher pay for women's work.

Lately, I have been avoiding the term comparable worth because it has given the opposition an opportunity for obfuscation and evasion. Those of us who are campaigning to clean sex bias out of the payroll should flush our adversaries out from behind the foggy comparable worth jargon to meet us head-on with arguments relevant to our demand for higher pay for female-dominated occupations. We should require them to explain why they foresee an end to civilization as we know it if Mom gets a fair share of her own apple pie.

A cheap shot? Not when my objective has been characterized as "the looniest idea since Looney Tunes" (the chair of the U.S. Civil Rights Commission) and "pregnant

(continued on page 23)

Karen Place is business representative for the International Federation of Professional and Technical Engineers, Local 17, AFL-CIO.



approved the Equal Pay Act, it specifically rejected language which would have required equal pay for "comparable" work.

Four Key Elements

First, comparable worth is based on comparing dissimilar jobs—secretaries to truck drivers, for example. It is not equal pay for equal work. Since pay equity is a matter of personal perception, how do you establish to a legal certainty that secretaries are worth more than truck drivers or vice versa? The proponents say that you set up a committee (each member with his own set of biases), award points for each job attribute, and "voila"—comparable worth.

Second, it compares these dissimilar jobs based on their so-called "intrinsic" value. In other words, comparable worth totally disregards the labor market. What the proponents fail to acknowledge is that jobs *do not* have an intrinsic or absolute value. In a free market, wages are not taken as judgment of the inherent value of a worker. Jobs are an exchange between an employer who needs work done and a person willing to do the work. The "value" of this exchange in a free society is the amount the person who needs the service is willing to pay for it, and the amount the person able to do the work is willing to accept.

Third, it presumes an unbiased, objective job evaluation system can be created to determine the value of different jobs. Suffice to say, no such system exists. In an oft-cited study about comparable worth, a National Academy of Sciences panel observed: "We do not believe that the value. . .or worth. . .of jobs can be determined by scientific methods. Hierarchies of job worth are always, at least in part, a reflection of values." No universal standard of job worth exists because any definition of the relative worth of jobs is, in part, a matter of values and because, even for a particular definition, problems of measurement are likely.

A perfect example of how various job evaluators rank jobs differently is the comparison of job worth points for five job categories in Wisconsin, Iowa, Minnesota, and Washington.

The chart below shows that while three states rated licensed practical nurses higher than electricians, Minnesota rated them considerably less. In Wisconsin, the job evaluation system ranked dental assistants more valuable than electricians, while in Minnesota they were worth only half of what electricians were to be paid.

Fourth, it requires some third-party involvement to make the final determination of what a job is worth. Comparable worth advocates are constantly expressing their criticisms of the current market-based pay practices of both the public and private sectors. They contend that the labor market reflects past discrimination against women and, therefore, cannot be relied upon to set fair wage rates. The answer they propose would, therefore, require the imposition of the value system of some outsider (such as a court agency, arbitrator, or job consultant) who is not familiar with and does not understand the employer's system of values. Professor Donald Schwab of the University of Wisconsin, a nationally recognized expert on job evaluation, testified in June 1984 before the U.S. Civil Rights Commission that "achievement of comparable worth objectives through job evaluation would require substantial regulatory involvement in the pay setting practices of firms."

The Earnings Gap

Why has comparable worth become such a controversial issue? It comes down to three words: "the earnings gap." The earnings gap is the overall earnings differential between the average working woman and the average working man. Women's earnings as a percentage of men's have hovered in the 50 to 60 percent range for most of the century and, for a long time, comparable worth proponents have rallied around the slogan "fifty-nine cents." Recent figures show that by the first quarter of 1984, women's earnings as a percentage of men's rose to approximately 60 percent. This growth trend is confirmed in a recent study by Rand Corporation which predicts that women's wages relative to men's are going to increase dramatically over the next two decades.

In fact, the change in women's roles over the past two decades has already affected the earnings gap more than appears in gross statistics. Substantial progress has been made in bringing more women into higher paying jobs. These gains are being obscured by the recent influx of young and relatively inexperienced women into the workforce at

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Job Worth Points as a Percentage of Points Assigned to Electricians

	WI	IA	MN	WA
Electrician	100	100	100	100
Licensed Practical Nurse	150	124	79	108
Dental Assistant	108	77	50	73
Telephone Operator	91	64	49	60
Data Entry Operator I	55	72	43	63

with the possibility of disrupting the entire economic system of the United States of America" (a federal judge).

Such overheated rhetoric evolves from a distortion of what the so-called comparable worth movement is doing. It misconstrues it as a demand for the government to compel all employers to set wages according to a formula of "job worth" derived from a point-factor job evaluation method. The notion is attacked on various grounds, most commonly with charges that this would bring a disastrous intrusion of bureaucrats into business and industry, and virtually overthrow the competitive market system which is the foundation of our economy.

My opponents have no cause to portray pay equity advocates as coming after the whole economic structure with bulldozers when in fact we are using more precise instruments to change only one specific feature of the economy. Nobody is calling for a government-enforced, wholesale application of job evaluation techniques as the wage standard for the entire nation. We are not trying to overthrow the market system; we are simply trying to tinker with the market to achieve a more equitable result.

Some critics express outrage at the mere fact of the women's movement trying for direct intervention in the workings of the marketplace, but I do not acknowledge this as a legitimate criticism. Who does not try

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to manipulate the market? Every economic interest group capable of scraping a few dollars together has a program to influence the legislative and regulatory activities of government. It is hypocritical for organizations with mega-buck political action budgets to admonish women to have faith in the "free market" to produce fair wages for their labor. Mom is tired of waiting for her apple pie in the sky by and by.

There are really only two relevant, arguable issues: (1) whether low pay rates for predominantly female occupations are a product of the job characteristics (work which would be low paid no matter who the workers were), or a product of unfavorable bias against women's work; and (2) if sex bias is a factor in wage rates, how should the bias be corrected?

I am being generous even to concede that the first issue is arguable at this late date. No one has ever produced a reasonable alternative to sex bias to account for the

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Comparable Worth and Pay Equity

The term "comparable worth" seems first to have appeared in a 1951 resolution of the International Labor Organization, calling for equity between salaries in male and female dominated jobs. The United States ratified this resolution. During debate on the Equal Pay Act of 1963, there was considerable discussion as to whether "equal" or "comparable" should be used; equal was

In 1974, the first study was done in the United States designed specifically to look at the nature of the differences in wages between men's jobs and women's jobs using a point factor job evaluation system. This study, conducted on jobs in the civil service system of the state of Washington, was called a comparable worth study. The term "comparable worth" has stuck and is used to refer specifically to the use of job evaluation to measure that part of the salary gap between men and women not attributable to differences in effort, skill, responsibility, and working conditions.

While comparable worth is still used by some to refer to all of the overall gap in wages between men and women, in the last few years "pay equity" has become the term of choice in this context. This difference in meaning and use is especially important to some unionists because of their longstanding opposition to job evaluation systems. Job evaluation is seen by these people as a management tool historically used to thwart bargaining for wages and to justify management practices. To them, any wage adjustments, including those to redress sex discrimination, should be negotiated through collective bargaining, not through the imposition of a job evaluation system. Pay equity, then, incorporates the salary gap that a comparable worth study measures, but does not depend upon such a study in a specific setting to justify adjustments since all studies to date using a variety of systems in a variety of settings show consistently the same results, pay equity advocates say, so more job evaluation study is necessary.

Comparable worth appears primarily in the public sector, and for several reasons. The public sector usually has restrictions on collective bargaining, most often prohibiting negotiations of wages. Civil service systems lend themselves to job evaluation studies because of the already accepted bureaucratic structure, employee access to classification information, and the inability of employees to change wages through collective bargaining. Further, only in the public sector is there free access to wage data, so necessary for conducting the studies preliminary to comparable worth, demonstrating the ever-present sex segregation and wage differentials. Lastly, the public sector is open to public pressure on elected officials, groups other than employees have an avenue for influencing the pay policies of the employer.

The private sector is most likely to feel pressure for pay equity from women—either those in place or in the form of unionization drives, especially for clerical workers. By whatever name, the idea that at least part of the wage gap between men and women is unfair now has wide acceptance. To many, what is left to be decided is not whether women are or have been unfairly treated, but how to remedy it. Comparable worth and pay equity have proven to be excellent organizing slogans: employers can choose to wait for unionization and collective bargaining, to wait for federal or state laws, or to begin addressing obvious problems in their pay structures now. This issue is not going away.

—Helen Remick, Ph.D.

entry levels. Until they acquire more seniority and job skills, their participation will tend to perpetuate the earnings gap.

There is an earnings gap—no question about that—but there's also an information gap. There's very little understanding of the underlying causes of the male/female earnings differential. As a result, a major concern is that unsound solutions will be adopted before the true nature and dimensions of the problems are understood. We're concerned that employers will be saddled with the burden of redressing not just that part of the earnings gap that *might* be attributed to discriminatory employment practices. Will they also be held responsible for disparities that stem from discrimination in education and from other societal and cultural factors outside the employment context? To the extent that women are concentrated in low paying jobs because of broader cultural and social factors and not because of discrimination in hiring assignments or promotions, we should be looking for solutions that address the real causes, rather than treating the symptoms through arbitrary wage adjustments.

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The Case in Washington State

Army Manseth, assistant vice-president for Pacific Northwest Bell and a member of the Joint Select Committee appointed by the Washington state legislature to make recommendations on implementing comparable worth in state salaries, makes the following observation on the committee's recommendations. "The committee recommended full implementation of comparable worth be completed no later than the end of the 1989–91 biennium and 50 percent of the total appropriation be appropriated in the 1985–87 biennium. They also recommended initial salary increases to bring employees up to the 'average comparable worth line' and the legislature give serious consideration to full implementation of comparable worth by increasing salaries to the 'male comparable worth line.' They made these recommendations in spite of the fact that they were dealing with a study by Norman Willis that was ten years old, that evaluated only 3 percent of the state's job classifications, and that was seriously flawed because certain aspects of 'working conditions' and 'accountability' were not taken into account. In addition, no consideration was given to the fact that the state might be overcorrecting for disparities unrelated to sex discrimination . . . that some part of the pay gap between female and male dominated jobs was attributed to societal and cultural factors."

Dr. Daniel Glasner of Hay Associates, a job evaluation firm, concludes that implementing comparable worth would have a major inflationary impact. Using the comparable worth advocates' favorite figure of sixty cents on the dollar and their claim that only twenty cents of the difference can be explained by nondiscriminatory factors, he estimates the total price tag to eliminate the remainder of the gap to be $320 billion. Some will argue that when you're dealing with alleged discrimination, the price tag is irrelevant, but effects of this magnitude cannot be ignored.

Fred Bowen, director of personnel for Boeing's Customer Services Division, and the company's focal point for comparable worth, states: "Implementation of any domestic social policy, and that's what comparable worth is, without facing the economic realities of the international marketplace we must operate in would have disastrous effects. To raise labor costs without an attendant increase in productivity is inflationary and would result in a deterioration of our market position."

Bowen also points out some of the practical problems that companies would encounter in trying to implement a comparable worth system. "We have a payroll of approximately 95,000 employees. We are located in every state and in forty-eight countries around the world. Our employees are represented by thirteen unions and their affiliates with both local and nationwide contracts. Our people represent every college discipline and every degree level. These complexities raise some interesting questions.

- What will be the makeup of the job evaluation committees? Since wage setting represents a major concern of the unions, do you have a cast of thousands on those committees, each with their own set of biases?
- How do you deal with domestic versus overseas assignments?
- How do you deal with job comparisons that cross union jurisdictional boundaries?"

Against

The Equal Opportunity Approach

Comparable worth represents a giant step toward central economic planning. It means the federal or state government gains direct control over the most intimate and crucial part of the economy—*the employment relationship*. It will retard women's steady progress towards true equality and occupational integration and will price many lower skilled women out of the market.

Private sector companies have been taking steps for over twenty years to increase job mobility for women through their affirmative action programs. It is possible to eliminate the earnings gap over time as sexual stereotypes change and by pursuing a policy of vigorous enforcement of existing nondiscrimination laws, including the Equal Pay Act and Title VII of the Civil Rights Act of 1964. This will ensure that women truly do have complete equality of job mobility, women and men receive equal compensation when they work in equal jobs, and victims receive a full remedy whenever there is proof that there has been intentional sex discrimination in setting pay rates.

An equal opportunity approach to the earnings gap problem won't provide a solution overnight. It won't be "right now" as Judge Tanner demanded in the State of Washington court case. But when the costs and benefits of the possible alternative are fully considered, the equal opportunity approach appears to offer the only effective solution that is consistent with our existing economic system and social values.

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Comparable Worth Down Under

When Australia adopted "equal pay for equal value" legislation in 1972, the cost of implementation raised considerable concern. But according to Jocelyene Clark of Australia's Office of the Status of Women, "It hasn't been disastrous at all." Moreover, studies indicate that from 1969 to the present, women's participation in the Australian workforce climbed from 30 percent to almost 40 percent, while their wages increased more than those of women in any other developed nation.

Comparable worth covers all governmental and most private sector employees in Australia, but the legislation has not been fully implemented because of price and wage controls that tend to perpetuate the status quo. Additionally, 90 percent of the increase in female participation in the labor market is attributed to part-time jobs, which have attracted many married women back to the workforce. On average, Australia's women earn about 80 percent as much as Australia's men, which is better than their female counterparts in the United States where the figure is sixty cents on the dollar.

Although obstacles confronting women in the Australian marketplace are similar to those faced by women here, the government and private sector have made it somewhat easier for women to balance the demands of home and job Down Under by providing maternity leave, child care services, and flexible working hours.

consistent and substantial disparity in wages between jobs done mostly by women and jobs done mostly by men. The "human capital" characteristics of the workers do not explain it, and the effects of supply and demand do not explain it. A blue-ribbon National Academy of Sciences panel of experts, having reviewed masses of national data on occupations and wages with state-of-the-art number-crunching, concluded that the sex composition of an occupation does indeed exert a powerful influence on the wage rate, and the more an occupation is dominated by women, the less it pays (*Women, Work, and Wages*, National Academy Press, 1981). The prevailing pay alignments in the labor market, and pay alignments within individual work organizations, reflect a longstanding social consensus that whatever women do is inferior to and worth less than whatever men do.

As to the question of how to correct this bias, the action programs now underway bear no resemblance to the comparable worth bogeyman (bogeywoman?) who is supposedly coming to rip apart our economic institutions. To begin with, nearly all the action is in the public sector and addresses only the way government agencies establish pay alignments for their own workforces. There is no army of bureaucrats mobilizing to invade private firms.

It is a sensible and workable strategy to place direct action campaigns within the public sector. Government is and should be responsive to claims based on a principle of equity, and governments can adapt to changes in their positions in the labor market without facing a threat to their viability. Governments do not have to compete for an economic niche.

Since I have alluded to the possibility of economic risk, I must dispose of another of the opposition's scare stories, namely that equitable pay for women's work will be an unmanageable cost burden. The recent pay equity program in the state of Minnesota represented a 4 percent increase in payroll costs and a 2 percent portion of the total state budget, and was accomplished without new taxes. The estimated cost of full implementation of Washington's comparable worth legislation is less than 2 percent of the budget, and implementation will be phased in over several years. I have no idea how some people generate cost estimates in the billions, and on what grounds they predict horrendous inflation rates, massive layoffs and unemployment, and other nasty consequences.

The prevailing pay alignments...reflect a longstanding social consensus that whatever women do is inferior to and worth less than whatever men do.

Most pay equity programs are specific, targeted corrective actions, not radical overhauls of the whole compensation system. The remedy is tailored to the problem. The problem is that women's jobs are unfairly underpaid, so the remedy, obviously, is to raise the pay. Job evaluation methods are used as a diagnosis, not as a cure. The technique produces data on how much of the pay variance within a particular organization is due to sex bias, as distinguished from legitimate variances based on job characteristics. The anticomparable worth carping about the undesirability of setting wages according to a rigid evaluation formula is beside the point because it does not happen that way.

If enough government entities in key labor markets raise the wages they pay for female-dominated occupations, there will be an effect on private firms. That is what pay equity advocates hope for. We are using action campaigns to change public sector compensation practices as a lever to raise pay rates in the wider market. To the extent we succeed, the effect on the private sector will be indirect, incremental, and will arrive with plenty of advance warning. American business has always prided itself on innovation and adaptability to changing conditions. Business will adapt to conditions generated by the claims of the underpaid female labor force if it ignores the comparable worth panic-mongers and pays attention to real world events.

Those who want to view something with alarm ought to consider this: the great majority of the poor in America are women and their dependent children, and *two out of every five* households headed by women are in poverty. Some of these are the working poor in the low paid female-dominated service and clerical jobs, earning wages but still qualifying for food stamps and other public assistance. Can we keep on using the fiction that "women do not have to support families" to justify inequitable wages for women's work? Is the public interest well served by maintaining a growing population of public dependents when some significant portion of the bill is a subsidy of private labor costs?